Province of British Columbia
Ministry of Finance and Corporate Relations

FINANCIAL INSTITUTIONS ACT

Major Policy Proposals

October 20, 1988

FINANCIAL INSTITUTIONS ACT

MAJOR POLICY PROPOSALS

Table of Contents

CHAPTER	TITLE	PAGE
1	Introduction	1
2	Incorporation, Reorganization and Winding-Up of Financial Institutions	5
3	Business Authorization and Business of Financial Institutions	11
4	Capital Requirements	15
5	Deposits and Liquidity	19
6	Ownership	23
7	Management of Financial Institutions	27
8	Reporting and Audit	31
9	Investment and Lending Standards	35
10	Shares and Membership in Credit Unions	39
11	Related Party Rules	43
12	Marketing of Financial Products	47
13	Regulation of Insurance Agents and Adjusters and Role of the Insurance Council	51
14	Regulation of Insurers	57
15	Regulation of Extra-Provincial Corporations	61
16	Administration of Financial Institutions Act	65
17	Offenses and Penalty Provisions	69

CHAPTER 1

INTRODUCTION

PURPOSE

The purpose of this document is to provide a summary of the major policies which are currently expected to be embodied in the consolidated financial institutions legislation slated for introduction and debate in the Spring, 1989, session of the British Columbia Legislature. This is essentially a description of the current state of the draft legislation under the working title of the Financial Institutions Act (FIA). It should be noted that these policies have not received final government approval and are subject to change as the result of further consultation and the Cabinet review process.

This document continues the consultation process which has been ongoing since the initiative was announced in November, 1986, and which included release of the discussion paper on amendments to the Credit Union Act, as well as a paper outlining major insurance policy initiatives. The government's policy intentions have become increasingly specific and detailed as the major principles and policies of regulatory reform are debated in British Columbia, across Canada and around the world. Also, as the legislation itself is drafted, there is an interaction between legal/drafting issues and policy issues which often highlights and clarifies the approach.

Although many of the details will continue to be refined, the policies described in this paper are intended to be consistent with the broad policies which have been announced over the past two years.

MAJOR OBJECTIVES

The ultimate objective of the FIA is to provide an up-to-date and effective regulatory framework which facilitates the operation of financial markets and financial institutions in British Columbia while providing enhanced public protection.

The major policy objectives which underlie the new legislation include:

- the incorporation procedure should be relatively simple, allow only bona fide institutions to incorporate, and be uniform across institutions;

MAJOR OBJECTIVES (Continued)

- legislation should be flexible, especially investment and lending rules and business powers, to allow British Columbia firms to diversify and be competitive, while providing safeguards for customers;

- increased reliance should be placed on the directors, officers and auditors of financial institutions;

- comprehensive rules should regulate transactions with related or non-arms' length parties and deal with conflict-of-interest situations;

- a comprehensive approach to the marketing of financial products should include rules to permit the cross-selling of financial products (except insurance), to require adequate disclosure, to prohibit tied-selling and to restrict the use of the terms "deposit" and "guarantee";

- the roles of Cabinet, the Minister and the Superintendent of Financial Institutions should be made more consistent and reasonable, with Cabinet approving regulations, the Minister making major decisions which require consideration of the public interest and the Superintendent responsible for day-to-day administration; and

- there should be comprehensive and effective enforcement powers, consistent with a graduated approach to requiring compliance with the Act, and balanced by a fair appeal process.

ORGANIZATION

The FIA will provide the regulatory framework for the operation of trust corporations, insurers, credit unions, insurance agents, and insurance adjusters. It will replace the Trust Company Act and the Credit Union Act in their entirety, as well as those provisions of the Insurance Act which regulate insurers.

The primary reasons for taking this approach are:

- to apply consistent policies and, where appropriate, identical provisions to all provincially regulated financial institutions. As the legislation is amended over time, consistency will be maintained more easily with the consolidated approach than with the separate Acts; and

ORGANIZATION (Continued)

- to permit the Legislature to deal with this major reform of all three pieces of legislation simultaneously.

It has been suggested that differences between institutions are so fundamental that consolidated legislation does not make sense. These differences are rapidly being eroded by market forces. Nevertheless, the legislation will treat different kinds of institutions differently where appropriate. For example, the unique corporate structure of credit unions will be recognized and maintained.

There may be some concern that the legislation will be difficult to use, requiring users from one part of the financial sector to wade through a lot of irrelevant material. The legislation will be organized to mitigate that concern.

The FIA will consist of "parts", each of which may be comprised of "divisions" which are ultimately made up of "sections". The FIA will have parts which roughly correspond to the chapters in this document, organized on functional lines. Within each part, the divisions will each apply to one or more kinds of institution. For example, Division 1 of the part devoted to "Incorporation, Significant Changes and Winding-Up", may be "Incorporation of Trust and Insurance Companies" and each section in the division will apply to both trust and insurance companies. Division 2 may be "Winding-Up of Insurance Companies" and each section will apply only to insurance companies. Division 3 may be "Incorporation and Significant Changes of Credit Unions". It will be clear to users which divisions are of interest and applicable to them.

Parts related to central credit unions and to credit union deposit insurance will be included in the legislation but are not discussed in this document. In both cases, apart from minor drafting changes, the legislation will be essentially the same as provisions in the Credit Union Act. No substantive policy changes are intended at this time.

The following chapters which outline the major policy proposals contained in the FIA are designed to be read at any of three levels of detail, depending upon the interest of the reader. The first section of each chapter is a brief description of the general policy; the second section is a discussion of the rationale for the chosen policy; and the third section is a more detailed elaboration of the policy approach to be taken in the FIA.

TERMINOLOGY

The FIA will use some terminology not commonly in use in existing legislation. This document follows the FIA terminology. Most of the terms are described in the relevant chapters. Terms which are used throughout and which may be unfamiliar include:

"business authorization" replaces licence for insurance companies and registration for trust companies;

"financial institution" means a trust company, insurer or credit union incorporated in British Columbia;

"superintendent" means the Superintendent of Financial Institutions. At present, this is only a title of convenience, since one individual is the Superintendent of Insurance, the Superintendent of Credit Unions, and the Superintendent of Trust Companies. Under the new Act, there will be only one Superintendent;

"trust company" includes what is sometimes referred to as a loan company in other jurisdictions (that is, a company which accepts deposits and makes loans but does no trust business).

CHAPTER 2

INCORPORATION, SIGNIFICANT CHANGES AND WINDING-UP

POLICY

The FIA will establish a two-stage procedure for the formation of financial institutions. The first stage will be the incorporation of a limited company or credit union. Incorporation will require the consent of the Superintendent, followed by consent of the Minister. The second stage will be the issuance of a business authorization (see Chapter 3). Provisions for credit unions will differ from those for trust and insurance companies in recognition of the unique corporate structure of credit unions. However, the provisions will be generally similar, based on the same underlying principles and a consistent process.

The consent of both the Superintendent and the Minister will also be required for fundamental corporate changes, such as amalgamations or compromises.

The provisions of the Company Act dealing with winding-up and dissolution will apply to all financial institutions. However the Minister, Superintendent and the deposit insurer will be granted some authority over the winding-up of individual institutions. The priority of those with claims against a financial institution being wound-up will be clarified to the extent possible.

DISCUSSION

The principal advantages of the FIA provisions are:

- Incorporation procedures will be simpler, and will eliminate unduly restrictive barriers to entry. However, incorporation of a financial institution will clearly be a privilege, not a right. Administrative procedures will attempt to ensure that only financial institutions with a reasonable chance of success and which will be operated in a prudent and appropriate way will be incorporated.

- The two-stage process gives a financial institution time to get organized using its status as a legal entity to contract for space, raise capital, etc., before beginning operations. For those not requiring such time, it may be possible to qualify for a business authorization very quickly following incorporation.

DISCUSSION (Continued)

- The provisions regarding corporate reorganizations will ensure that a financial institution has enough flexibility to adopt the most efficient structure, while ensuring that the public interest will be protected, consistent with the incorporation provisions.

- Because the framework for winding-up financial institutions will be the same as for other provincial companies, there will be increased certainty regarding the dissolution of these institutions. Uncertainty and inconsistency in the priority system will also be reduced.

DETAILED APPROACH

Incorporation

Incorporation of proposed trust and insurance companies will be carried out pursuant to the provisions of the Company Act. In keeping with the objective of increasing flexibility, the FIA will not contain any restrictions as to who may incorporate a financial institution.

However, before the Registrar of Companies may register an incorporation, both the Minister and the Superintendent must consent. The Superintendent must be satisfied that:

- the procedural requirements have been met;

- the proposed memorandum and articles of the institution are appropriate; and,

- the business plan outlining the financial services to be offered and the preliminary activities to be undertaken complies with the Act.

An appeal to the Commercial Appeals Commission from the Superintendent's decision will be permitted.

The Minister may approve the incorporation if the Superintendent has given his consent and the Minister believes the incorporation is not contrary to the public interest.

Although different procedures will exist for the incorporation of credit unions, the FIA will modify existing requirements in the Credit Union Act to make them more uniform with the requirements facing insurance and trust companies. This will include transferring corporate registry responsibilities for credit unions to the Registrar of Companies. The approval process for

DETAILED APPROACH (Continued)

credit union incorporation will be identical to that for other financial institutions, requiring Superintendent's consent based on satisfaction of administrative requirements, followed by ministerial approval if incorporation is not contrary to the public interest. As with other financial institutions, business authorizations will be required before business commences.

Since a credit union is cooperative in nature, the FIA will require that at least 25 persons subscribe in order to apply for incorporation and that all subscribers must reside in the province and share a common bond. Furthermore, a credit union will not be incorporated under the Company Act, but will be incorporated pursuant to provisions set out in the FIA although, where appropriate, Company Act sections will be applied.

The use of names, including phrases such as "trust", "insurance" and "credit union", will be restricted to avoid the public being misled. Financial institutions which have not yet been granted a business authorization will be required to use the phrase "[Not Authorized]" whenever they use their name.

The Trust Company Act and the Insurance Act both contain requirements that deposits be maintained with the government. In light of deposit insurance and insurance compensation plans, no similar deposit requirements will be included in the FIA.

Significant Changes

Significant changes, including compromises and arrangements with creditors and amalgamations of trust and insurance companies, will also proceed under the Company Act. This includes amalgamation by any method including purchase of assets or statutory amalgamation. Trust and insurance companies will only be permitted to amalgamate with other trust companies and insurance companies respectively, or with their own subsidiaries. The consent of both the Minister and the Superintendent will be required prior to significant changes, based on the same criteria and process as applied to incorporations.

Different provisions for corporate reorganizations of credit unions will take account of their cooperative nature and of the role of the Credit Union Deposit Insurance Corporation (CUDIC).

A credit union will be able to sell either all its shares or all its assets to another credit union or to a trust company. The latter will be the mechanism to allow conversion to a trust company. Consistent with the Credit Union Act, the purchaser of

DETAILED APPROACH (Continued)

a credit union's assets will be required to assume the liabilities of the credit union and to pay the fair market value for equity shares. A share purchase will require the purchase of all of the credit union's equity and non-equity shares. When a trust company is involved under either method of purchase outlined above, approval of both the Superintendent and three-quarters of the credit union's members will be required for the transaction to proceed. However, CUDIC will be able to exercise the powers of the members and the Superintendent for a credit union under supervision.

A statutory amalgamation between two credit unions will follow the existing Credit Union Act provisions. CUDIC will retain the right to exercise the powers of the members of a credit union under supervision.

Winding-Up

Provisions for the voluntary or Minister-ordered winding-up of solvent financial institutions will be included in the FIA.

Sections applicable to all financial institutions will allow the Minister to order an institution to be wound-up for serious infractions which endanger the public (operating without a business authorization or without deposit insurance), either before a business authorization is granted or after it is revoked. The Superintendent will be able to apply to the court for orders binding on the receiver or liquidator. There will be requirements for filing quarterly reports, and applications for winding-up or a change of liquidators with the Superintendent.

The FIA will also contain sections applicable only to insurance companies. Provisions similar to those in the current Insurance Act will require a liquidator of an insurance company to attempt to purchase reinsurance and pay out the various claimants.

The FIA will also contain winding-up provisions specific to credit unions. CUDIC, as both the deposit insurer and the stabilizer of financially troubled credit unions, will be able to order the winding-up of credit unions under supervision and appoint a liquidator or act as liquidator for any credit union being wound-up. CUDIC will continue to have the power to assume the assets and liabilities of a credit union.

DETAILED APPROACH (Continued)

The winding-up of trust companies will also require special provisions. Unlike the deposit insurer of credit unions, the deposit insurer of trust companies, Canada Deposit Insurance Corporation (CDIC), is not involved in stabilization. Consequently, CDIC will not have the right to order winding-up or appoint a liquidator. However, it will have the same right as a creditor to apply to the court for these orders.

Priority Provisions

The federal government has constitutional responsibility for bankruptcy and insolvency. The federal Winding-Up Act deals with insolvent trust companies, credit unions and insurers. However, that Act provides only sketchy priority provisions for trust companies and credit unions, but relatively complete provisions for insurance companies.

For insurance companies, it is proposed that the Winding-Up Act (Canada) provisions be relied upon.

To reduce uncertainty in the winding-up of trust companies and credit unions, whether insolvent or not, priority provisions will be set out in the FIA consistent with, but more complete than, the provisions of the Winding-Up Act (Canada). The proposed provisions for trust companies and credit unions are that the proceeds of liquidation would be paid in the following order:

- costs of liquidation and secured creditors;
- depositors and non-equity shareholders of credit unions (including the deposit insurer to the extent that depositors have been paid out);
- unsecured creditors;
- subordinated note holders (see Chapter 4); and
- equity shareholders.

CHAPTER 3

BUSINESS AUTHORIZATION AND BUSINESS OF FINANCIAL INSTITUTIONS

POLICY

Following incorporation (see Chapter 2), a financial institution must satisfy the requirements to be granted a business authorization by the Superintendent of Financial Institutions before commencing business and offering financial services to the public. A business authorization is evidence that the financial institution has presented a feasible business plan, met specified prudential safeguards and satisfied regulatory requirements.

DISCUSSION

At present, an insurance company is incorporated and then licensed under the Insurance Act before it may engage in insurance business. A trust company is incorporated and then registered under the Trust Company Act. A credit union is incorporated pursuant to the Credit Union Act and, immediately upon incorporation, may engage in deposit and loan business and trust business. The FIA rationalizes these processes.

The business authorization requirements will be more clearly set out in the FIA than in the existing Acts. These requirements will ensure that the Superintendent has a full opportunity to assess the viability of the business plan of a financial institution and be satisfied that selected prudential safeguards can be met before the provision of financial services is commenced.

DETAILED APPROACH

Business of Financial Institutions

The FIA will give all financial institutions full corporate powers - the powers of a natural person - subject to the restriction that a financial institution engage only in the business of providing financial services.

In addition, certain types of business will be restricted to financial institutions which hold a valid business authorization. Specific prohibitions will make it illegal for:

- any person (corporation or individual), except a bank, to engage in deposit and loan business without a business authorization;

DETAILED APPROACH (Continued)

Business of Financial Institutions (Continued)

- any person except a licensed insurance agent, an authorized society, a permitted reciprocal exchange, a registered captive insurance company, CUDIC, CDIC and recognized insurance compensation plans to engage in insurance business without a business authorization; and,

- any corporation, except a law corporation, to engage in trust business without a business authorization.

Deposit and loan business will be defined as the business of offering to the public the service of receiving money on deposit that is intended to be lent or invested by the person with whom it is deposited, and is repayable to the person making the deposit on demand, after notice, or on the expiry of a specified term.

Trust business means providing or offering to provide services to the public as trustee, executor, administrator, guardian of a minor's estate, or committee of a mentally incompetent person's estate. Trust companies will be able to rely on their natural person's power to undertake other related activities (i.e., stock transfer agent) and are not limited by this relatively narrow definition of trust business.

Insurance business means providing or offering to provide services to the public to indemnify a person against loss or liability for loss in respect of a certain risk or peril to which the object of the insurance may be exposed or to pay a sum of money or provide another thing of value on the happening of a certain event.

Business Authorization

Before commencing business, a financial institution must obtain a business authorization from the Superintendent. A credit union may apply for a business authorization to engage in deposit and loan business and/or trust business. A trust company may apply for a business authorization to engage in deposit and loan business (savings and loan company), trust business (a company offering purely fiduciary services) or both (a full service trust company). An insurance company may apply for a business authorization to engage in either life insurance, general insurance, or both.

DETAILED APPROACH (Continued)

Business Authorization (Continued)

If a financial institution has not applied for and been granted a business authorization within one year after the date of its incorporation, the Minister will order that the financial institution be wound-up. A financial institution may apply to the Minister for one 6-month extension. At any time before a business authorization is granted, the Minister may reconsider his decision to allow incorporation and order that the financial institution be wound-up.

Financial institutions in operation prior to proclamation of the FIA will be deemed to hold a valid business authorization, subject to (in the case of trust companies and insurance companies) any conditions on their former licence or registration.

In the case of credit unions currently offering trust business, a business authorization for trust business will not be automatic. If the Superintendent is satisfied that a credit union offered trust business prior to the Act coming into force and has the financial and managerial capacity to carry on trust business, the Superintendent will issue a business authorization to a credit union to engage in both deposit and loan and trust business.

To be granted a business authorization, a financial institution must satisfy the Superintendent that:

- it has an adequate capital base to support its proposed business operations (see Chapter 4);
- it has at least five directors and, in the case of a trust or insurance company, at least one-third are unaffiliated directors;
- its proposed plan of operations is feasible; and,
- it is insurable or approved by the appropriate deposit insurance corporation or a member of the appropriate insurance compensation plan.

A business authorization will contain any general conditions prescribed by regulation and may also contain conditions set by the Superintendent. The Superintendent may amend or remove any conditions he has attached to a business authorization and may, at any time, place new or further conditions on the business authorization of a financial institution.

DETAILED APPROACH (Continued)

Business Authorization (Continued)

A business authorization is continuing; a financial institution will not be required to renew an authorization on a periodic basis.

When a financial institution ceases to engage in business in the province, is voluntarily wound-up, or makes a written application, the Superintendent may revoke its business authorization. Refer to Chapter 16 for a discussion of the policy respecting revocation of a business authorization as a result of regulatory action.

CHAPTER 4

CAPITAL REQUIREMENTS

POLICY

British Columbia proposes to take a flexible approach to the issue of capital requirements. The primary requirement in the legislation will be that each financial institution authorized to do business in the province maintain a capital base which is adequate to support its business activities, subject to minimum capital levels imposed for trust and insurance companies. This general requirement will be augmented by capital adequacy tests imposed by regulation.

While it will be necessary for financial institutions to meet the minimums and any other prescribed requirements, the Superintendent will have discretion to consider all relevant factors in determining if capital is adequate in any particular case. The onus will be on the financial institution to maintain an adequate level of capital. Where the Superintendent judges capital to be inadequate, the Superintendent will be empowered to restrict dividends and share redemptions and require remedial action.

DISCUSSION

The capital of a financial institution should be sufficient to reduce the risk of insolvency to an acceptable level. However, there are significant costs associated with acquiring and maintaining capital. Capital requirements should not be so onerous as to impede the growth and development of financial institutions.

The practical result of the primary requirement that every financial institution maintain adequate capital will be that institutions with approximately the same amount of assets under administration but engaged in different business activities could have different capital base requirements. Institutions engaged in riskier businesses will have to maintain relatively larger capital bases.

This approach provides flexibility to achieve a reasonable balance between the dual goals of protection against insolvency and limiting impediments to financial institution development. By relating capital requirements to business risk and providing the flexibility to address this on a case-by-case basis, the approach will help ensure that the capital cushion is adequate in any particular instance. Adoption of minimum capital levels for trust and insurance companies provides consistency with other jurisdictions and relevant deposit insurance and insurance compensation fund requirements.

DETAILED APPROACH

Definition of Capital Base

Capital base will be defined in regulations to the Act as prescribed assets less prescribed liabilities. This approach provides flexibility to define capital base consistently with the capital adequacy rules imposed. For example, consideration will be given to excluding capital that is devoted to fixed assets but subordinated notes that meet certain criteria may be included in the base. Specific provisions in the FIA will set out the criteria and rules associated with subordinated notes.

Trust and Insurance Company Minimums

The legislation will set the following minimum capital requirements:

- $1.5 million for insurance companies engaged in general insurance business;
- $3 million for insurance companies engaged in life insurance business;
- $3 million for trust companies engaged only in deposit and loan business; and,
- $5 million for trust companies engaged in both trust business and deposit and loan business.

No minimum will apply to trust companies engaged only in fiduciary business.

New companies must meet the minimums prior to receiving a business authorization. Existing companies will be given a transitional period of five years to comply.

Other Prescribed Requirements

The legislation will allow for the prescription in regulation of additional specific capital requirements. Specifically, consideration will be given to prescription of risk-weighted capital/asset ratios for each type of financial institution, similar to the BIS requirement for international banks. Assets and off-balance-sheet exposures such as guarantees would be weighted to reflect the associated risk and the resulting value compared with the capital base. This will facilitate a better estimation of the degree to which any institution's capital base is sufficient. As with the minimum capital requirements, prescribed ratio requirements will serve as prerequisite conditions which will not override the Superintendent's discretion to judge the adequacy of the capital base.

DETAILED APPROACH (Continued)

Other Prescribed Requirements (Continued)

Prior to adopting a risk-weighted capital/asset test, capital adequacy tests will be adopted for credit unions which approximate the current statutory reserve account (SRA) requirement, except that the concept of SRA will be replaced by capital base. Trust and insurance companies may have limits prescribed (for example, 5 per cent minimum capital/asset ratio for trust companies and life insurance companies and 3:1 maximum net premium revenue to capital ratio for general insurers).

Compliance

The legislation will prohibit the payment of dividends or the redemption of shares by any financial institution where payment would reduce the capital base below an adequate amount.

In addition, a financial institution that has failed to maintain an adequate capital base may be required by the Superintendent to take remedial action. In the case of credit unions, inadequate capital will continue to be a primary trigger for supervision by CUDIC.

CHAPTER 5

DEPOSITS AND LIQUIDITY

POLICY

Credit unions and trust companies authorized to engage in deposit and loan business will be required to maintain adequate liquidity as prescribed by regulation. For credit unions, there will be mandatory pooling of liquidity with B.C. Central Credit Union, subject to a liquidity formula. Provisions will be included to deal with unclaimed deposits, similar to existing and proposed federal provisions.

Credit unions will be limited, consistent with current provisions, to accepting deposits from members and certain specified persons.

DISCUSSION

Only corporations that are members of an approved deposit insurance agency, and which are specifically authorized, should be permitted to offer to the public deposit and loan business. This is an essential public protection.

Financial institutions which engage in deposit and loan business must, in turn, have adequate liquidity in order to maintain depositor confidence. At present both trust companies and credit unions must maintain a certain percentage of "liquid" assets in order to meet their ongoing, immediate financial obligations. The FIA will continue this requirement because liquidity is essential for the stability of individual financial institutions and the entire financial sector.

DETAILED APPROACH

Deposit-taking

The FIA will contain a specific prohibition against any person, other than a bank, trust company, credit union or extra-provincial trust corporation with a business authorization from engaging in deposit and loan business. As outlined in Chapter 3, a key requirement for obtaining a business authorization to engage in deposit and loan business is that the institution is eligible to have its deposits insured by a recognized deposit insurance agency.

DETAILED APPROACH (Continued)

Deposit-taking (Continued)

Similar to the provisions in the existing Credit Union Act, a credit union will only be able to accept deposits from:

- its members;
- the government of the Province or Canada;
- a public body (which includes a municipality, government body as defined under the Financial Administration Act, and any board or commission undertaking specific public programs);
- a partnership where a majority of partners would qualify as members;
- a member in joint ownership with another person; and,
- a member or other person acting as a trustee.

Unclaimed Deposits

If there has been no account activity for 10 years, a deposit will be declared an "unclaimed deposit". If the unclaimed deposit is less than $100, the trust company or credit union will retain it and treat it as income; if the unclaimed deposit is over $100, it will be passed over to the government for inclusion in the Consolidated Revenue Fund. A depositor will have five years after the deposit becomes an unclaimed deposit to make a claim if the deposit has been retained by a trust company or a credit union, and 20 years to make a claim if the deposit has been transferred to the government.

Liquidity

The FIA will require a trust company or credit union that is authorized to engage in deposit and loan business to maintain liquid assets as prescribed.

A trust company will be required by regulation to maintain liquid assets equal to 10 per cent of its liabilities. Liquid assets will be defined as cash, certain demand and term deposits and investment in certain government bonds, notes and commercial paper.

A credit union will also be required to maintain 10 per cent liquidity. However, as a further requirement, this liquidity will have to be maintained with B.C. Central Credit Union,

DETAILED APPROACH (Continued)

Liquidity (Continued)

subject to a liquidity formula. A credit union will be required to keep liquidity on deposit at B.C. Central up to a maximum of 10 per cent of B.C. Central's total assets. Required liquidity in excess of that limit will be subject to rules consistent with the rules for trust companies.

The FIA will require every credit union to become a member of B.C. Central by subscribing to a nominal amount of share capital of B.C. Central.

CHAPTER 6

OWNERSHIP RESTRICTIONS

POLICY

A variety of restrictions could be placed on the ownership of financial institutions, including restrictions on non-resident ownership and closely-held ownership. British Columbia has never placed these types of restrictions on the ownership of trust or insurance companies and will not change that policy at this time.

However, consistent with the basic objective of promoting the development of the financial sector while providing improved public protection, the Minister will have the power to disapprove or set conditions on the acquisition or transfer of shares, which results in an owner obtaining or increasing a significant interest (10 per cent or more of the voting shares) in a trust company or insurance company.

DISCUSSION

British Columbia does not support financial/commercial ownership restrictions, rules requiring financial institutions to be widely held, or foreign or non-resident ownership restrictions. Such limitations establish unnecessarily restrictive barriers to entry into the financial sector.

As a counter-balance, comprehensive prudential safeguards are provided in other parts of the FIA. These include provisions regarding self-dealing and conflicts of interest and the requirement for unaffiliated directors. To these is added a policy of ministerial review of significant ownership changes. This will be an effective safeguard against the risks that unrestricted ownership may generate for the stability of the financial sector. The policy is consistent with the policy of requiring ministerial approval for incorporation and for substantial corporate changes.

It is intended that persons acquiring the shares of a trust company or insurance company should find the rules straightforward and easy to comply with but difficult to evade.

DETAILED APPROACH

General Provisions

All individuals and corporations (including holding corporations) which, together with persons in the group described below, acquire or increase a significant interest in a trust company or an insurance company, must obtain the prior approval of the Minister. For the purposes of this provision, the group includes:

- a corporation which the individual or corporation controls and every affiliate of the corporation;
- a partner of the individual or the corporation, where each of the partners has at least a 10 per cent beneficial interest;
- a trust or an estate in which the individual or corporation has a 50 per cent or greater beneficial interest or for which the person is a trustee; and
- in the case of an individual, the spouse of the individual and any relative of the individual or spouse, who shares the same home.

Due to the cooperative nature of credit unions, no similar restrictions are required. Current credit union provisions requiring most members to qualify within the credit union's common bond will be retained, with additional exemptions as proposed by the credit union movement.

Criteria for Refusal of Consent

The Minister may refuse to consent to the share acquisition or transfer where he is satisfied that the person acquiring the shares:

- is or has been bankrupt;
- has been convicted of an offense under the Criminal Code which indicates that the person should not be in a position to influence the affairs of an insurance or trust company;
- has been convicted of an offense under the FIA or the Securities Act or other similar legislation in other jurisdictions;
- is or has been subject to a cease trading order under the Securities Act or other similar legislation;
- is the subject of an investigation under the FIA or other similar legislation;

DETAILED APPROACH (Continued)

Criteria for Refusal of Consent (Continued)

- is in contravention of or has contravened the provisions of this Act or other similar legislation;
- has failed to comply with an undertaking given to the Superintendent;
- has failed to provide requested information;
- is a mentally disordered person; or
- is otherwise, in the opinion of the Minister, a person who ought not to be in a position to influence the affairs of a trust company or an insurance company (i.e., it is contrary to the public interest to give consent).

Other Provisions

The Superintendent, the trust company or the insurance company will have the power to require shareholder ownership declarations and other information from persons who own shares of the company directly or indirectly. The company will also have the power to establish by-laws requiring persons holding voting shares of the company to submit ownership declarations designed to establish actual beneficial ownership of the companies.

A "flutter rule" to deal with relatively small share transfers or acquisitions will be included. Transfers or acquisitions within a band of plus or minus 5 per cent from an approved ownership level will not require approval. For example, if an individual or a corporation owns 30 per cent of the voting shares of a trust company or insurance company, ownership interest may be decreased to 25 per cent and then increased up to 35 per cent, without requiring approval of the Minister.

An individual or a corporation may apply to the Minister for prior approval to increase their ownership position substantially over a set period of time. This provision permits an acceptable person to gain control of a financial institution without returning repeatedly to the Minister for approval of acquisitions that make up the program.

CHAPTER 7

MANAGEMENT OF FINANCIAL INSTITUTIONS

POLICY

The FIA will enhance the responsibilities of directors and officers of financial institutions. The standard of care of directors and officers will be clarified and increased slightly, consistent with other jurisdictions. The responsibilities of directors and officers to manage the affairs of the financial institutions will be significantly expanded.

DISCUSSION

Directors and officers play a critical role in the strategic direction and operational management of any organization, including financial institutions. There is no substitute for an effective board of directors and management team and, accordingly, the FIA relies on directors and officers to manage the financial institution.

Generally, provisions respecting directors and officers in the FIA parallel other jurisdictions' financial institutions legislation reform proposals. A basic reform principle across Canada is to strengthen the internal corporate governance requirements in financial institutions legislation.

DETAILED APPROACH

Unaffiliated Directors

A financial institution will be required to have at least five directors and, in the case of a trust company or an insurance company, one-third of all directors must be "unaffiliated directors".

An unaffiliated director is an individual who is not:

- an employee of the financial institution or his or her spouse, or a relative occupying the same home;
- a former affiliated director or employee of the financial institution (two-year limit);
- an individual who holds more than 5 per cent of the voting shares of a financial institution or his or her spouse or a relative who occupies the same home;

DETAILED APPROACH (Continued)

Unaffiliated Directors (Continued)

- a director or employee of a significant borrower of a financial institution or a significant owner of a significant borrower of a financial institution or his or her spouse; or,

- the holder of a loan not in good standing from the financial institution, or a significant owner of a corporation that has a loan not in good standing, or his or her spouse.

A quorum of the board of directors will require at least one unaffiliated director.

Board Committees

The directors of a financial institution will be required to constitute at least three committees:

- an investment and lending committee (see Chapter 9);

- an audit committee (see Chapter 8); and,

- a conduct review committee which is responsible for reviewing related party transactions and establishing conflict-of-interest guidelines (see Chapters 11 and 12).

In the case of trust and insurance companies, two-thirds of the conduct review committee members must be unaffiliated directors, and at least one-third of the directors composing the investment and lending and audit committees must be unaffiliated directors.

Standard of Care

The standard of care for directors and officers will be increased from "reasonably prudent person" to "reasonably prudent person under comparable circumstances".

Qualifications

Where the Superintendent determines that a director or officer of a financial institution is no longer qualified to hold that position, he may order the removal of the director or officer. A director or officer may be removed from office:

- for contravening an undertaking given to the Superintendent;

- due to a conflicting interest that prevents him from properly discharging his duties as director or officer; or

DETAILED APPROACH (Continued)

Qualifications (Continued)

- because the Superintendent is satisfied that he is otherwise not fit or competent to be the director or officer of a financial institution.

The Superintendent will have the power to require information as necessary from the financial institution regarding directors and officers.

The Superintendent must be notified of any changes in directors or officers and upon election or appointment. A director or officer will be required to provide to the Superintendent a detailed personal information form, similar to the information form required under the Securities Act.

Resignation/Removal

A director who resigns, receives notice that he is to be removed from office or learns that his name will not be put forward for re-election, has the right to submit a written statement to the financial institution outlining his reasons for resigning or his reasons for opposing any proposed action. A financial institution will be required to send a copy of this written statement to every shareholder or member entitled to vote.

Where a director resigns as a result of a disagreement with the directors or management of the company, the director shall submit to the Superintendent a written statement outlining his reasons for resigning.

Provisions Respecting Directors that are Specific to Credit Unions

A credit union will be permitted to include provisions in its rules to have up to three professional directors who are not members of the credit union and are appointed by the board to provide additional technical expertise.

A director of a credit union will be required, unless exempted by the Superintendent, to successfully complete a prescribed training program within six months of election to the board of directors.

DETAILED APPROACH (Continued)

Provisions Respecting Directors that are Specific to Credit Unions (Continued)

To provide for absentee voting for the election of directors and special resolutions, a credit union with more than 10,000 members or that has a branch office which is located more than 40 kilometers from any other branch office, will be required to provide either mail balloting, in-branch balloting, or both.

CHAPTER 8

REPORTING AND AUDIT

POLICY

The FIA will enhance the role of the external auditor in relation to financial institutions. A key aspect of this new expanded approach is the establishment of clear reporting relationships between the external auditor, audit committee, directors and the Superintendent. The Superintendent will have the power to order the removal of an auditor if he is unable to meet the requirements of being an auditor of a financial institution.

DISCUSSION

Auditors can and do play a significant role in the corporate governance of a financial institution. External auditors provide a professional, objective and independent assessment of a financial institution's financial activities and position. While the primary output of this assessment is a set of audited financial statements, auditors are in a unique position to detect and identify policies, procedures and programs which may adversely affect the financial institution.

Often, it is a lack of information, not resolve, that prevents directors (or officers) from dealing with emerging difficulties. This is a major reason that the role of the auditor is being strengthened.

DETAILED APPROACH

Reporting and Financial Statements

Every financial institution will be required to produce annual audited financial statements. The financial statements must be prepared on a consolidated basis where the financial institution has subsidiaries or is a subsidiary of a holding company that controls other financial institutions. This will ensure that there is no double counting of capital in determining capital adequacy.

The external auditor will generally be required to follow generally accepted auditing standards (GAAS) in making his examination and report and financial statements will generally be required to be in accordance with generally accepted accounting principles (GAAP). The legislation will enable GAAS and GAAP to be supplemented with specific requirements or standards.

DETAILED APPROACH (Continued)

Audit Committee

All financial institutions will be required to establish an audit committee, with one-third of the members required to be unaffiliated directors in the case of trust and insurance companies. The audit committee will be required to meet at least twice each year to review prescribed matters including financial statements prior to approval and release by the board and returns to be filed with the Superintendent.

Every five years, the audit committee will be required to appraise the work of the auditor and recommend to the board whether the appointment should be continued.

The auditor, a member of the audit committee, or another director, will be able to call a meeting of the audit committee at any time. In addition, the auditor has the right to attend and be heard at meetings of the directors or other board committees on any matter of direct relevance to the auditor.

Mandatory Reporting and Access to Information

In making his examination, the auditor will be provided with broad statutory access to information from past and present directors, officers and employees of the financial institution.

An auditor who, in the normal course of his duties, becomes aware of a change in the circumstances of a financial institution that might have a material and adverse effect on the financial institution, or that a director or officer has not complied with the Act, will be required to report the matter to the board of directors of the financial institution.

If the board of directors has not responded to the auditor's report or taken corrective action within 30 days of receiving the report, the auditor will be required to report the matter to the Superintendent.

There will also be provision for the correction of errors in annual statements or returns on the initiative of the auditor or a director.

Removal or Resignation

A financial institution will be required to notify the Superintendent of any change in the office of auditor.

The Company Act provision respecting the removal of an auditor will be adopted. Under this provision, an auditor who is being removed from office has the right to make a written statement and

DETAILED APPROACH (Continued)

Removal or Resignation (Continued)

the financial institution must forward a copy of this statement to every member or shareholder entitled to vote. An auditor who resigns from office must submit to the financial institution and the Superintendent a statement of the reasons for his resignation. The financial institution will be required to give a copy of the statement to the replacement auditor.

The Superintendent may order the removal of an auditor if he is satisfied that the auditor has

- failed to perform his duties;
- failed to comply with the Act; or,
- been party to the preparation of, or has approved, a financial statement that does not fairly present the position of the financial institution.

An auditor removed by the Superintendent will not be eligible to be reappointed by the financial institution without the permission of the Superintendent. The Superintendent will also be able to specify that an auditor removed in this manner must also be removed from the position of auditor of any other financial institution.

Further Provisions

The Superintendent may require the auditor of a financial institution to:

- report more fully on the adequacy of financial management procedures followed by the financial institution;
- enlarge the scope of the audit;
- submit additional information relating to the financial affairs and operation of the financial institution;
- apply principles in addition to or instead of GAAP and GAAS.

The Superintendent will have the power to order, where he considers it necessary and desirable, that an additional or second auditor be appointed for a financial institution. This

DETAILED APPROACH (Continued)

Further Provisions (Continued)

additional auditor will carry out the duties of auditor of the financial institution independently of any other auditor.

In both of the above cases, the additional costs of the audit will be borne by the financial institution.

CHAPTER 9

INVESTMENT AND LENDING STANDARDS

POLICY

The objective of the new investment and lending standards is to provide more flexibility for investment and lending to financial institutions by eliminating qualitative restrictions replacing them with a prudent portfolio concept. Appropriate diversification of investment and loan portfolios will be part of the prudent portfolio requirement. If necessary diversification could be imposed by establishing quantitative caps on particular loan and investment categories through regulations.

There will be provision for extensive cross-ownership of financial institutions and other financial service corporations as a means of effectively broadening business powers but still keeping different businesses separate for regulatory purposes.

DISCUSSION

Existing British Columbia legislation contains specific and detailed qualitative investment criteria which narrowly restrict the investment powers of British Columbia financial institutions. Qualitative rules are considered ineffective and unnecessarily restrictive.

Investment and lending rules should be flexible enough to allow financial institutions to manage their assets with the objectives of maximizing return and minimizing risk to optimize the portfolio.

It is proposed that qualitative investment criteria be replaced with a prudent investment portfolio concept and provision for quantitative limits for specific investment and lending categories. This approach is consistent with the federal approach and will afford financial institutions considerable flexibility and new business opportunities.

DETAILED APPROACH

Prudent Portfolio Requirement

Every financial institution will be required to manage its financial assets (investments and loans) to comply with a prudent portfolio standard. The prudent portfolio standard is defined as the standard employed by a prudent person making and managing loans and investments on behalf of another person to whom there is owed a fiduciary duty of care.

DETAILED APPROACH (Continued)

Prudent Portfolio Requirement (Continued)

The responsibility for ensuring the prudent portfolio standard is met rests with the board of directors. In order to accomplish this, a committee of at least three directors and officers, at least one of whom is an officer with investment and lending responsibility, will be required (the investment and loan committee). In the case of trust and insurance companies at least one-third of the committee members will have to be unaffiliated directors.

This committee will be required to prepare for board approval a written investment and lending policy designed to satisfy the prudent portfolio standard. A copy of the current policy must be provided to the Superintendent each year as part of the financial institution's annual report filing. If the Superintendent does not feel that the institution's written policy is prudent or that the proposed criteria for dealing with a certain type of investment or loan (for example, real estate) is not prudent, the Superintendent may order that the policy be reviewed or altered.

The Lieutenant Governor in Council will have the ability to specify quantitative limits on investments and loans to supplement the prudent portfolio requirement. Initially, there are no plans to use this power but if the prudent portfolio approach alone is not effective quantitative limits may be specified.

A limit will be set (per cent of capital base) on the amount which may be lent to or invested in one person (individual or corporation) and its associates. Consideration is being given to a limit of the greater of 25 per cent of the capital base, consistent with the federal proposal, or one per cent of assets.

Investment in Affiliates

Consistent with the general requirement that financial institutions engage only in the business of providing financial services, there will be a general prohibition against owning more than 10 per cent of the shares of most non-financial corporations. The FIA will include a specific list of corporations in which more than 10 per cent ownership is permitted subject to the ownership approval requirements described in Chapter 6 where applicable. These corporations will include:

- banks;
- insurers and insurance agencies;

DETAILED APPROACH (Continued)

Investment in Affiliates (Continued)

- trust corporations;
- investment dealers, investment counsellors, portfolio managers;
- international financial business corporations;
- mutual fund corporations;
- financial leasing corporations;
- factoring corporations;
- credit card corporations;
- venture capital corporations;
- real estate, property management and land development corporations;
- data processing corporations;
- corporations which primarily provide services to the financial institution and its affiliates; and,
- financial service corporations specified in regulation.

Where the financial institution has one or more subsidiaries or is the subsidiary of a holding corporation that controls other financial service corporations, investments and loans shall be combined with those of the financial institution for the purposes of assessing whether the prudent portfolio standard has been met.

A financial institution will be able to acquire more than 10 per cent of an otherwise ineligible corporation under certain conditions - for example, exchange for debt as the result of the reorganization of a debtor, in an amalgamation or other restructuring of the financial institution, or as the result of realizing on security for a loan. Superintendent's approval will be required in some cases and such shares will have to be disposed of within five years.

The Superintendent will have the power to require the disposal of investments which do not comply with the Act and regulations.

CHAPTER 10

SHARES AND MEMBERSHIP OF CREDIT UNIONS

POLICY

The FIA will improve the ability of credit unions to issue equity shares in order to raise capital to support their business operations.

To achieve this end, it is proposed that a two-tiered share/membership structure be established in legislation. Credit union members will be required to own a nominal amount of qualifying shares of their credit union in order to take full advantage of membership benefits. These shares would not be covered by deposit insurance and would be redeemable only upon withdrawal from membership. Thus, qualifying shares will differ from both equity and non-equity shares.

A credit union will be able to issue equity shares to members or non-members of the credit union, but when a non-member purchases equity shares that person will automatically become an "auxiliary member" with very limited rights. Non-equity shares will continue to exist without change (see Comparison of Share Types on Page 42).

DISCUSSION

At present, a credit union may only offer equity shares to its members. This has restricted the ability of credit unions to raise capital. A financial institution must be adequately capitalized to support risk and its investment activities.

The approach to be adopted in the FIA enhances credit unions' ability to raise capital in the open market by allowing equity shares to be issued and transferred to non-members.

Membership is then distinguished by having a share purchase requirement as a condition of membership. This is done by specifying a type of share (qualifying share) which may only be issued or transferred to members. It is not unreasonable to require members of a credit union to own shares in their credit union. Credit union legislation in other Canadian jurisdictions includes this type of requirement.

DETAILED APPROACH

Qualifying Shares

Every member of a British Columbia credit union will be required to subscribe to a minimum number of qualifying shares as a condition of membership. The minimum amount ($5) will be set in legislation, but a credit union will be permitted to set a higher amount in its rules. A par value will be required for qualifying shares. Qualifying shares will not be guaranteed by CUDIC and will participate in the proceeds of liquidation only up to their par value. Credit unions will have a one-year transition period in which to comply with the new requirements.

Many credit unions already have a program of mandatory membership shares. Generous transitional provisions will be included in legislation to facilitate the conversion of existing shares into "qualifying shares". The intent is to make compliance with this new requirement as easy as possible.

Equity Shares

The FIA will enable credit unions to issue equity shares as authorized by their rules. The rules of a credit union shall specify the number of shares in the class, whether or not the shares have a par value and, if so, the par value and any special preferences, rights, restrictions or conditions attached to the shares. Similar to existing legislation the directors of a credit union may determine the payment of dividends on any class of shares (including the payment of a dividend by the issue of fully paid equity shares). As well, legislation will continue to permit the rules of a credit union to specify that dividends shall be paid on one class of shares in preference to another class of shares, and that the rate of dividend paid on one class of shares may be different from that paid on another class of shares.

Equity shares may be sold to and transferred between members and non-members. However, a non-member purchasing equity shares of a credit union automatically receives the designation of "auxiliary member". Auxiliary members may attend meetings of the credit unions but are not entitled to vote on special or ordinary resolutions or the election of directors and may not hold any office in the credit union.

Equity shareholders, including auxiliary members, will have the right to vote on resolutions affecting any special rights attached to their shares. For the purpose of such a vote, the legislation will permit the credit union's rules to specify that each equity shareholder will be entitled to one vote per share.

DETAILED APPROACH (Continued)

Withdrawal from Membership and Termination

A member of a credit union may withdraw from membership by applying for the repayment of his qualifying shares and for the withdrawal of all money on deposit or invested in non-equity shares with the credit union.

Membership termination provisions similar to those recently included in the Cooperative Association Act will be included in the FIA. This essentially will give members terminated by the directors an appeal to the membership and protects the rights of the member.

The withdrawal or termination of a member is effective on the total repayment of all qualifying and non-equity shares and the total withdrawal of all money on deposit. The repayment of qualifying shares and withdrawal of deposits is subject to the completion of any term or condition of a term deposit and any claim the credit union has against the member for any outstanding indebtedness the member has to the credit union.

A member who holds equity shares in a credit union and who withdraws from membership or has his membership terminated automatically becomes an auxiliary member. Auxiliary members may deal with equity shares as they wish, subject to the rights and restrictions associated with the shares.

Alternative Voting Procedures

Based on the concept that persons with a significant equity position in an institution should have some say in substantive decisions of the institution, it has been suggested that an alternative voting procedure be considered for credit unions.

One option is to allow a credit union to provide in its rules that each member have one vote per equity share for all special resolutions of a credit union. This would include special resolutions of a credit union to change its name, amend its common bond, alter its constitution and rules, amalgamate with another credit union, buy the assets or shares of another credit union or trust company, or sell its assets or shares to a credit union or trust company. Auxiliary members would not have a vote, except as described above. The principle of one member/one vote would be retained for all ordinary resolutions and for the election of directors.

DETAILED APPROACH (Continued)

Comparison of Share Types

	Qualifying	Equity	Non-Equity
Par Value Required	Yes	No	Yes
Multiple Share Classes	No	Yes	No
Eligible for Dividends	Yes	Yes	Yes
Condition of Membership ($5 minimum)	Yes	No	No
Issue/Transfer to Auxiliary Members (non-members)	No	Yes	No
Redemption on Termination of Membership	Yes	No	Yes
Participates in Equity on Winding-up	No	Yes	No
Priority on Winding-up	Before Equity Shares	Last	With Deposits
Insured by CUDIC	No	No	Yes

CHAPTER 11

RELATED PARTY TRANSACTIONS

POLICY

The purpose of related party rules is to protect the interests of consumers and the public by preventing non-arm's length transactions that threaten a financial institution's solvency.

British Columbia proposes to take the following approach to the regulation of related party transactions:

- The definition of related party will encompass all parties with the potential to control or significantly influence a financial institution's decision-making. The concept will extend beyond parties with direct control to those with substantive linkages with the financial institution;

- Related party transactions will not be prohibited, but all related party transactions will be required to be consistent with usual business practice, approximate market value, conform with specified aggregate value limitations and be in the best interests of the financial institution;

- The onus will be placed on the board of directors of the financial institution to ensure that these conditions are met for potentially damaging related party transactions; and,

- Certain high-risk, related party transactions will be permitted only with the approval of the Superintendent of Financial Institutions.

- Remedial actions and sanctions will be sufficient to provide an effective incentive for compliance by financial institutions, their boards of directors and related parties.

DISCUSSION

British Columbia's approach differs significantly from that of the federal, Quebec and Ontario governments. That legislation tends to ban all related party transactions subject to specified exceptions, some of which require approval of the board of directors of the financial institution. Alberta intends to adopt the general ban approach as well.

The British Columbia approach directly addresses the problem of potential abuse of influence while also recognizing that related party transactions occur in and are necessary to the everyday

DISCUSSION (Continued)

business of financial institutions. In so doing, it strikes an appropriate balance between the need to constrain related party influence and the need to avoid unreasonably restricting the operations of financial institutions. The approach also provides the flexibility necessary to ensure that the application of the related party rules to any particular situation results in a reasonable outcome. It is consistent with the general principle that the role and responsibilities of the boards of directors of financial institutions for internal corporate governance should be increased. In addition, by placing the responsibility for ensuring compliance in the first instance on the financial institution, the approach avoids imposing a regulatory duty that cannot reasonably be met without substantial additional resources.

Because the approach is not consistent with that being taken elsewhere, it could add to the difficulties financial institutions face in meeting differing regulatory requirements. It will, however, be considerably easier and less expensive for financial institutions to comply with British Columbia's approach than with the general ban approach. These provisions will also apply for the most part only to British Columbia incorporated companies.

There may be a public perception that the approach proposed in British Columbia is not adequate to constrain abuses of influence. This reflects the assumption that the potential for abuse will be greater under a more self-regulatory scheme. It can, however, be reasonably argued that self-policing, in combination with significant sanctions on non-compliance, is a more effective means of ensuring that potential abuse is identified and avoided. On the other hand, a general ban will be extremely difficult to police, is likely to promote the development of innovative methods for evasion by those intent on unscrupulous behavior, and will tempt good corporate citizens to break the law in order to proceed with standard business transactions.

DETAILED APPROACH

Definition of Related Party

Related party rules will apply to all transactions with parties who can exercise control or significant influence upon the decisions of financial institutions. This corresponds generally to the Company Act concept of a corporate insider and encompasses the following:

- directors, officers, auditors and actuaries of the financial institution and certain members of their immediate families;

- persons who directly or indirectly own 10 per cent or more of the voting shares of the institution; and,

DETAILED APPROACH (Continued)

Definition of Related Party (Continued)

- persons with an indirect link through related corporations of which they own 50 per cent or more of the voting shares.

Additionally, in order to meet unanticipated situations, the Superintendent will be empowered to designate persons as related parties where sufficient grounds exist.

Process of Reviewing Transactions

Related party transactions, other than those specifically exempted by the legislation, will be subject to review by a committee of the board of directors of the financial institution - the conduct review committee.

In the case of trust and insurance companies, two-thirds of the members of the conduct review committee will have to be unaffiliated directors. Committee members will be required to meet disclosure and conflict-of-interest rules in the conduct of their duties.

The onus will be on the conduct review committee to approve only those transactions that are consistent with usual business practice, approximate market value, and are in the best interests of the financial institution. In the case of transactions with a subsidiary, the market value test will not apply since financial statements will be prepared on a consolidated basis making the price of such transactions irrelevant.

Certain high-risk forms of related party transactions such as real estate and security transactions will be permitted only with the approval of the Superintendent. Security transactions involving share transfers or acquisitions approved by the Minister under the policy requiring ministerial review of significant ownership changes (see Chapter 6) will be exempt from this provision.

Additionally, certain loan and asset acquisition and disposal transactions which exceed prescribed aggregate value levels will be prohibited outright. Others, which are part of a corporate restructuring, will be subject to Superintendent's approval.

Transactions Not Subject to Review

Certain types of related party transactions will not require committee approval. These transactions are sufficiently nominal that review is not warranted, involve the provision of services at market value that are part of a corporation's ordinary business with the public, or are adequately vetted in some other manner.

DETAILED APPROACH (Continued)

Disclosure Requirements

To ensure transactions are reviewed with full knowledge of the situation, related parties who are party to actual or proposed transactions with financial institutions will be required to disclose their interest in writing for the records of the board of directors. Directors who are party to any such transaction will be barred from any proceedings of the board which deals with the matter and will be prohibited from exercising any influence upon the review process.

Remedial Actions and Sanctions

To respond to non-compliance with any of the related party rules, the Superintendent's enforcement powers will include the issuance of cease and desist orders, issuance of orders requiring remedial action and application to the Supreme Court to reverse the transaction. The court will be given broad powers to require any gain to be accounted for, compensation to be made and damages to be paid.

The recourse granted directors and members in the Company Act to sue on behalf of the financial institution will also be available to the Superintendent and, in the case of a credit union, to CUDIC. In this instance, the court will be empowered to require repayment of the full amount of the transaction or payment of damages to the financial institution.

Persons who knowingly approve, participate in, or facilitate a transaction which contravenes the related party rules will be jointly and severally liable for their actions. Contravention of the related party rules and failure to comply with an order made in this regard will be offenses subject to significant maximum penalties.

CHAPTER 12

MARKETING OF FINANCIAL PRODUCTS

POLICY

Networking of financial services and products will be permitted under the FIA except for the retailing of insurance. Networking means contractual arrangements between financial institutions whereby one entity sells directly to the public through its own outlets the financial products of other related or unrelated companies.

Comprehensive rules respecting disclosure, confidentiality and conflict-of-interest will be established in legislation. As well, the FIA will introduce rules to restrict the use of the terms "guarantee" and "deposit" by financial institutions when offering their services to the public.

DISCUSSION

The financial services industry in Canada is undergoing profound change. This market-driven change is resulting in an increasing array of financial products in the marketplace, to the benefit of consumers. The reorganization taking place in the financial services industry poses significant challenges for regulators. Existing legislation, which provides for regulation on an institutional basis, requires modification to appropriately deal with the sale of a diverse range of financial products by a single retail outlet and with other marketing innovations.

One response is to allow the cross-ownership of financial institutions (one financial institution holds or is held by other types of regulated financial institutions) including cross-ownership with a diverse array of companies offering financial-type services (see Chapter 9).

Another response is to allow for and regulate the networking of financial products. By allowing financial institutions to simultaneously market the products of other financial institutions under "one roof", significant economies of scale may be realized. The consumer could benefit from increased convenience and greater competition at the retail level.

On the other hand, the networking of financial products entails serious potential risks, including:

- confusion concerning the identity of the financial institution actually providing the product;

DISCUSSION (Continued)

- "tied-selling", where a customer's purchase of one financial service is explicitly or implicitly a condition on the purchase of another service or product;

- breach of confidentiality, where confidential customer information is disclosed to other areas of the organization or its affiliates, giving them a competitive advantage; and,

- conflict-of-interest, where the interests of two customers, or a customer and the financial institution may be in competition.

Therefore, the granting of networking powers to financial institutions must be balanced with strong prohibitions against tied-selling and the release of confidential information, measures to ensure full disclosure regarding the product the customer is buying and a mechanism to deal with conflicts of interest.

Recent events have suggested that when the expression "guarantee" or "deposit" is used in connection with a deposit or investment instrument, a customer assumes that the instrument is insured by an entity such as the Canada Deposit Insurance Corporation or otherwise protected by government backing. This may not always be the case, thus misleading the customer.

The elimination of such confusion is considered essential to the maintenance of confidence in the financial system and a necessary consumer protection. Accordingly, the use of the words "guarantee" and "deposit" will be limited.

DETAILED APPROACH

Disclosure Rules

A financial institution entering into a transaction with a customer will be required to disclose the identity of the corporation that is actually providing the financial product or service.

As well, the financial institution will be required to disclose to the customer:

- all direct and indirect corporate links which could have a bearing on the customer transaction;

- the existence (but not necessarily the amount) of any commission arrangements; and,

DETAILED APPROACH (Continued)

Disclosure Rules (Continued)

- an assurance that the customer is under no obligation to purchase any other specific service or product as a condition of this transaction.

Tied-Selling

Section 34 of the federal Competition Act is an explicit prohibition against tied-selling with substantial potential penalties. This federal legislation makes it illegal for a corporation to require, as a term or condition of a transaction, that a customer enter into a further transaction with the corporation.

This is a law of general application to both federal and provincial corporations. As well, the federal government has jurisdiction in the area of competition law. Thus, a specific prohibition against tied-selling in provincial financial institution legislation may be unnecessary and/or outside the jurisdiction of the province. Further research is being undertaken to determine the constitutionality of a tied-selling ban in the FIA.

Confidentiality

A financial institution will be prohibited from communicating to any other person confidential customer information for marketing or other purposes unrelated to the original reason the information was originally requested, without the consent of the customer. Information related to insurance contracts received by a trust company or credit union will be required to be held strictly confidential and not be released, even with the customer's consent.

Conflict of Interest

The FIA will require the conduct review committee of the board of directors to establish rules and procedures to resolve conflict-of-interest situations and to identify potential conflict-of-interest situations and develop procedures for preventing their occurrence.

Substitute Action by Superintendent

The Superintendent will have the power, with the consent of the Minister, to take legal action on behalf of customers who have been subjected to misleading, deceptive or unconscionable marketing practices of the financial institution. This provision is very similar to the representative action clause of the Trade Practices Act.

DETAILED APPROACH (Continued)

Limitations on Use of Terms "Guarantee" and "Deposit"

No person (financial institution, sales agent, advertiser, etc.) will be permitted to solicit investments or deposits from the public using the word "guarantee" or any derivative unless:

- the amount in question is insured to the maximum by CDIC or another prescribed insurer;
- it is guaranteed by an independent third party approved by the Superintendent;
- it is guaranteed by Canada or a province; or,
- the use of the word is authorized by regulation.

The use of the word "deposit" in relation to financial deposits or investments will be restricted to trust companies and credit unions authorized to engage in deposit and loan business and banks. This restriction will be designed not to affect non-financial deposits (i.e., a deposit on property being purchased, etc).

CHAPTER 13

REGULATION OF INSURANCE AGENTS AND ADJUSTERS AND ROLE OF THE INSURANCE COUNCIL

POLICY

The Insurance Council of British Columbia (the Council) is established by regulation and authorized to license and discipline insurance agents, salesmen and adjusters by virtue of powers delegated by the Superintendent of Insurance under the Insurance Act.

It is proposed that the Council be continued as a corporation under the FIA and that statutory powers be conferred on the Council, making it directly responsible for the licensing of agents, salesmen and adjusters and for the imposition on sanctions on these licensees. The provisions for the licensing of insurance agents and adjusters will be similar to those in the Insurance Act but consistent with the approach taken on business authorizations.

DISCUSSION

Self-regulatory organizations (SROs) offer the following advantages:

- administrative costs to government can be reduced since industry representatives on an SRO can provide a high level of expertise for minimal remuneration and expenses can be covered by assessments on the industry;
- self-regulation by members of the industry is more consistent with a free market economy since government intervention in the marketplace is lessened; and,
- members of SROs have a strong incentive to maintain educational and professional standards because this enhances the credibility of the industry as a whole.

The main potential problems with SROs are:

- educational and professional requirements could be used as a barrier to entry, thus concentrating the business in the hands of existing licence holders and preventing other individuals from entering the industry; and,

DISCUSSION (Continued)

- SRO members may find that their personal or financial interests conflict with their regulatory responsibilities, since they will often hold prominent positions in the industry which they regulate.

In the case of the Insurance Council, these difficulties are addressed by:

- providing the Superintendent with power to, prior to the consideration of a case, remove the case from the Council's jurisdiction or to appeal a decision of the Council to the Commercial Appeals Commission;

- requiring Council members to refrain from participating in regulatory decisions in which they have a personal or financial interest; and,

- maintaining a balanced Council, consisting of individuals from the various segments of the insurance industry.

DETAILED APPROACH

Incorporation of the Council

The Insurance Council of British Columbia will be continued as a corporation, in order to give it a recognized legal personality. This will ensure that the Council is legally able to conduct business in its own name.

As a corporation, the Insurance Council will be given all the powers of a natural person, which will allow the Council to perform the duties conferred on it under the Act and regulations.

Appointment of Council Members

The powers conferred on the Insurance Council will be exercised by its members who will continue to be appointed by the Lieutenant Governor in Council for two-year terms. The current representation on the Council by life and general insurance agents, life and general insurance companies and adjusters, will be continued.

Financing of Council Activities and Remuneration

The activities of the Council will continue to be financed by fee revenue received from applicants for initial licences and licence renewals. Revenue-sharing arrangements with the Superintendent under the Financial Administration Act will continue, ensuring that fee revenue which is surplus to the expenses of the Council will be remitted to the government. The expenditures of the Council will be subject to expenditure guidelines.

DETAILED APPROACH (Continued)

General Licensing Requirement

The requirement that sales of insurance products in British Columbia be conducted only by licensed agents and salesmen (i.e., employees of agents) or through direct marketing by authorized insurers will be continued. An insurance adjuster's licence will continue to be required for the settlement of any loss. Existing exemptions will be maintained.

Step Licensing

The Council will continue to set the educational and professional standards for licensees and will be given the additional power to issue restricted licences, formalizing the existing step-licensing scheme.

Binding Authority Requirement for Licensing

The current requirement that all general insurance agents be sponsored by an insurance company will be replaced by a requirement that every general insurance agent have at all times binding authority from at least one insurer. For this purpose, the Insurance Corporation of British Columbia (ICBC) will not be considered an insurer.

The binding authority requirement will help to ensure that consumers actually obtain the insurance protection they purchase, and will improve the market discipline imposed by the relationship between insurers and agents.

The existing requirement that life insurance agents be licensed as agent for a named insurer will be continued.

General Insurance Group Plans

The statutory authorization for the sale of group life insurance will not be expanded to facilitate the sale of general insurance group plans. Current restrictions on the sale of general insurance products will be maintained to ensure that consumers have access to properly trained insurance professionals.

Council Disciplinary Powers

The Council will be given direct authority to discipline licensees for:

- failing to continue to meet a requirement of licensing;
- making a material misstatement in an application for a licence or in a reply to an inquiry; or,
- failing to reply promptly to an inquiry.

DETAILED APPROACH (Continued)

Council Disciplinary Powers (Continued)

In addition to the existing penalties of cancelling, suspending or imposing conditions on a licence, the Council will be given the power to:

- require additional training;
- reprimand the licensee;
- issue a cease and desist order; and,
- levy a fine up to $2,000.

The Council will be required to investigate and to hold a hearing if one is requested prior to imposing sanctions.

On the completion of every investigation or hearing, the Council will be required to prepare a written report setting out its findings and the reasons for its decision, and shall provide the Superintendent and the licensee affected with a copy of the report.

Disciplinary Committees

The Council will be given direct authority to delegate disciplinary hearings to one or more committees composed of both members and auxiliary members of the Council. For this purpose, the Minister will be able to appoint any number of individuals as auxiliary members to serve on disciplinary committees.

Superintendent's and Minister's Powers

Currently, the Superintendent may withdraw a matter from the Council, prior to the Council's decision, and decide it in its stead. Alternatively, the Superintendent may appeal a decision of the Council to the Commercial Appeals Commission. These statutory safeguards will be maintained in the FIA.

The Superintendent will have the power to require the Council to establish written policies and to review these policies before they come into force. The Minister will have the power to give the Council policy direction, as long as it is consistent with their duties under the Act.

The Minister will be empowered to appoint a person to investigate or inquire into any aspect of the operation of the Council, including its financial affairs.

DETAILED APPROACH (Continued)

Superintendent's and Minister's Powers (Continued)

The Insurance Council will be required to provide the Superintendent upon request any information in its possession, including any records or books of account.

CHAPTER 14

REGULATION OF INSURERS

POLICY

There are two specific aspects of the operation of insurers which will be specially regulated under the FIA - reserves and reinsurance. The approach and the specific provisions are intended to be generally consistent with those proposed by the federal and Ontario governments.

There are a number of entities, other than insurance companies, which qualify as insurers and are regulated by the Insurance Act to some extent: societies, reciprocal exchanges and unlicensed (unauthorized) insurers. The FIA will continue to deal with these entities in a manner similar to current provisions, but consistent with the general approach of the FIA.

DISCUSSION

The Insurance Act currently contains limited provisions regarding reserves which insurance companies should maintain to cover the potential claims of policyholders and the unearned premiums which must be returned to an insured on the cancellation of a policy. Since inadequate reserves may ultimately lead to the insolvency of an insurer, it is important that statutory reserve requirements be expanded and updated to reflect modern accounting and actuarial principles.

The Insurance Act does not place any limits or restrictions on an insurer ceding reinsurance. However, if a reinsurer is unable to meet its obligations, the primary insurer will be affected. Insurers which reinsure heavily or reinsure mostly with "off-shore" reinsurers may be taking undesirable risks. For this reason, the federal government, Ontario and British Columbia are considering putting limits on the total amount of insurance which may be ceded to reinsurers and on the amount of insurance which may be ceded to unlicensed reinsurers.

One of the main objectives of the FIA is consistency of approach among institutions. For this reason, it is important that all insurers, whether they are companies, societies or reciprocal exchanges, have the same standards applied. It is also important that unauthorized insurers have only extremely limited scope for operation in British Columbia.

DETAILED APPROACH

Reserves

As far as practical, the specific reserve requirements will be consistent with or identical to federal provisions. These include:

- requiring an annual report by an actuary confirming the reserves;
- requiring that reserves of 115 per cent of "claims incurred but unpaid" and 115 per cent of "unearned premiums" be maintained; and,
- possibly detailing specific reserve calculations in the regulations.

Reinsurance

The FIA will include authority to enact regulations which limit the total amount of risk that can be reinsured and the amount of reinsurance that can be placed with unauthorized insurers. The regulations will parallel the draft reinsurance regulations proposed by the federal government. Specifically, an insurance company incorporated and authorized to do business in British Columbia will be precluded from reinsuring more than 75 per cent of the risk underwritten by it. These restrictions will be phased-in over four years for newly authorized companies and companies that are not in compliance when the regulations come into force.

In addition, an authorized insurance company will be precluded from reinsuring more than 25 per cent of the risks undertaken by it with insurers which are not licensed or authorized to do business somewhere in Canada. For these purposes, a company registered under the Insurance (Captive Company) Act will qualify as an authorized insurer. Again, this restriction will be phased-in over four years.

It is also proposed that an insurance company be required to notify the Superintendent prior to reinsuring with an associated corporation. This will give the Superintendent the opportunity to take action (see Chapter 15) where he believes the action would be an unsafe or unsound practice.

Certain pooling agreements entered into before a prescribed date which would not comply with the reinsurance regulations may be grandfathered.

DETAILED APPROACH (Continued)

Societies Engaged in Insurance

The Societies Act allows societies to be incorporated for the purpose of undertaking insurance under certain conditions. This will continue to be possible and insurers incorporated under the Societies Act will be treated exactly the same as insurance companies incorporated under the provisions of the FIA and the Company Act. That is, they will be subject to all the same requirements, including requiring a business authorization, capital adequacy rules, investment and lending provisions and annual inspection by the Superintendent.

The Insurance Act provides special provisions which effectively exempt a sub-set of societies which provide limited life insurance from regulation and which make the treatment of societies in general uncertain (sections 283 to 293). The spirit of these provisions will be retained but the provisions will be clarified so that it is clear that application is only to certain existing societies and no new societies will be regulated under the provisions.

Reciprocal Exchanges

Reciprocal exchanges are mechanisms for groups of insureds to pool risk by exchanging insurance contracts. Reciprocal exchanges will continue to be allowed subject to a requirement that a permit must be obtained from the Superintendent. The requirements for a permit will be similar to those for a business authorization. The Superintendent will be empowered to use the full range of his powers to regulate reciprocal exchanges.

Unauthorized Insurers

Similar to the Insurance Act, there will be no restriction on insuring with an insurer that does not hold a business authorization. However, an insurance agent will not be able to solicit insurance business on behalf of an unauthorized insurer and there will be a requirement that the insured remit 5 per cent insurance premium tax. The tax provisions related to unlicensed insurance in the Insurance Act will be moved to the Insurance Premium Tax Act.

If an unauthorized insurer needs to undertake activities in British Columbia with respect to insurance provided by that insurer on property in British Columbia (i.e., inspect a risk or adjust a loss), the insurer must first receive a permit from the Superintendent, as at present.

CHAPTER 15

EXTRA-PROVINCIAL TRUST AND INSURANCE COMPANIES

POLICY

Extra-provincial trust and insurance corporations will be covered by providing one division which references sections throughout the Act which apply to the extra-provincial corporation. The intent is to avoid duplication of regulation.

All extra-provincial corporations will be required to obtain a business authorization to operate in British Columbia.

The Superintendent will have access to sufficient information to take enforcement action if necessary against an extra-provincial corporation, but the regulator in the jurisdiction of incorporation will generally be relied upon as the primary regulator.

DISCUSSION

Other jurisdictions have taken two main approaches to the regulation of extra-provincial trust and insurance companies. In Ontario, the "equals" approach has been adopted, which requires an extra-provincial trust or insurance company to meet all the regulatory requirements of both Ontario and the province of incorporation.

New Brunswick has adopted the "designated jurisdiction" approach, which enables trust and insurance companies from designated jurisdictions to operate in New Brunswick after meeting certain basic requirements set by New Brunswick. Primary responsibility for regulation and administrative scrutiny is retained by the jurisdiction of incorporation.

British Columbia rejects the Ontario "equals" approach; the resulting double regulation is an unnecessarily cumbersome way to ensure effective regulation. Regulatory effort should be focussed where it is needed; that is, on trust and insurance companies from jurisdictions which do not have adequate regulatory safeguards. Accordingly, British Columbia plans to adopt the New Brunswick "designated jurisdiction" approach with modifications.

DETAILED APPROACH

Designated Jurisdictions

The Lieutenant Governor in Council will be empowered to designate jurisdictions if:

- the jurisdiction has legislation which establishes adequate regulatory procedures; and,
- a British Columbia trust or insurance company operating in the jurisdiction would be exempted in a similar manner.

The federal jurisdiction will be designated.

Application of Regulatory Provisions

An extra-provincial corporation from a designated jurisdiction will be required to apply for and obtain a business authorization. An extra-provincial trust or insurance corporation must meet the following requirements to be granted a business authorization:

- that it maintain adequate capital and meet any minimum capital requirements established by legislation (see Chapter 4);
- if it accepts deposits, it is a member of CDIC or an approved deposit insurer and if it is an insurer, it is a member of the appropriate insurance compensation plan;
- it is solvent and able to meet its business obligations as shown by its financial statements;
- it has a feasible business plan; and,
- it has appointed a British Columbia resident to act as its agent.

In addition to these business authorization requirements, an extra-provincial corporation from a designated jurisdiction will be subject only to the following provisions of the FIA:

- the Superintendent must be advised of changes to the position of auditor;
- financial information and returns must be provided to the Superintendent;
- requirements concerning the marketing of financial services must be complied with (see Chapter 12); and,
- administrative and enforcement powers will be available to the Superintendent.

DETAILED APPROACH (Continued)

Application of Regulatory Provisions (Continued)

An extra-provincial corporation from a jurisdiction that is not designated will, in addition to the above, be subject to FIA provisions concerning self-dealing, investment and lending standards, ownership and corporate governance.

All extra-provincial corporations operating in British Columbia will be required to maintain in a form acceptable to the Superintendent records of depositors, fiduciary activities, loans, investments and insurance contracts.

The extra-provincial corporation will be required to immediately notify the Superintendent of any changes of significance that occur outside British Columbia, including:

- a change in its licence, registration, charter or corporate structure;
- the commencement of an investigation or inquiry by another jurisdiction; or,
- any enforcement or compliance action taken against it.

In such circumstances, the Superintendent or the Minister will be empowered to take any enforcement action available under the FIA and/or revoke the business authorization.

The Superintendent must be advised of branch openings or amalgamation of extra-provincial trust or insurance companies. The latter will be subject to specified approval procedures.

Extra-provincial Operations of Credit Unions

Credit Unions do not operate extra-provincially in the same manner as other financial institutions since they are restricted to providing services within their province of incorporation. However, section 188 of the existing Credit Union Act allows the registration of an extra-provincial credit union for the purposes of perfecting or registering a secured transaction or maintaining a legal action. This provision will be retained in the FIA.

CHAPTER 16

ADMINISTRATION OF THE FINANCIAL INSTITUTIONS ACT

POLICY

The fundamental policy objectives are to:

- assign reasonable and consistent duties, powers and responsibilities to those responsible for making decisions under the Act - the Lieutenant Governor in Council, the Minister, the Superintendent, the Insurance Council and the Credit Union Deposit Insurance Corporation (CUDIC);

- provide a full range of sanctions which can be applied in a graduated manner to provide those not in compliance with the Act an opportunity to comply, but allowing fast, effective regulatory action when necessary; and,

- ensure balance by providing opportunities to those facing regulatory action to be heard and an effective, comprehensive and independent appeal process.

DISCUSSION

The intention is to limit the role of the Lieutenant Governor in Council to issuing regulations under the Act.

The Minister's role, in addition to approving incorporations, major corporate restructuring and significant ownership transfers is to make decisions regarding the cancellation of business authorizations as a regulatory sanction. The Minister will be able to provide CUDIC and the Insurance Council with policy direction, consistent with the existing Credit Union Act provisions. Neither the Minister nor the Superintendent will be able to take control of trust companies or insurance companies as the federal and Ontario legislation contemplates.

The Superintendent will be responsible for annual inspection and for taking regulatory action against financial institutions up to, but not including, cancelling business authorizations. Before taking action, the Superintendent is required to hold a hearing, if requested. In certain cases, if there is not time for a hearing before taking action, there is a procedure for holding a hearing and reviewing the decision after.

DISCUSSION (Continued)

The Insurance Council will be responsible for the licensing and regulation of insurance agents, adjusters and consultants (see Chapter 12). CUDIC will be responsible for regulation of credit unions under supervision and for commercial lending by credit unions until the current specific loan approval process is phased-out.

Appeals of all administrative decisions of the Superintendent, Insurance Council and CUDIC will be to the Commercial Appeals Commission. Decisions will not be stayed by an appeal unless the Commission orders a stay.

It is felt that this approach is internally consistent, places decisions at the appropriate levels, and contains adequate checks and balances to prevent abuse.

DETAILED APPROACH

Superintendent's Responsibilities

The Superintendent is appointed by the Minister and required to:

- maintain a register of financial institutions;
- inspect provincially incorporated financial institutions each year;
- make an annual report to the Legislature;
- keep information obtained confidential; and,
- give interested parties an opportunity to be heard before taking regulatory action.

Superintendent's Regulatory Powers

In addition to powers conferred elsewhere in the Act, the Superintendent has the power to:

- operate outside of British Columbia;
- inspect and require information at any time;
- address written inquiries to a financial institution;
- appoint an investigator with power to examine witnesses under oath;
- order a person to cease doing something or to do something if the person is not complying with the Act or is operating in an unsafe manner;

DETAILED APPROACH (Continued)

Superintendent's Regulatory Powers (Continued)

- enter into a voluntary compliance agreement with a person who is not in compliance with the Act;
- order property to be frozen;
- apply to the Supreme Court for an order for compliance with a Superintendent's order;
- require property, assets and insurance contracts to be appraised and require financial statement notes to disclose a value required by the Superintendent if different from the financial statement; and,
- apply to court for the appointment of a receiver when a business authorization has been revoked.

Minister's Regulatory Powers

In addition to the incorporation approval powers set out in Chapter 2, the Minister will have the power, on the report of the Superintendent that a financial institution has failed to comply with a Superintendent's order, a Commercial Appeals Commission order, or a court order or has committed a serious breach, to revoke the financial institution's business authorization.

Hearings and Appeals

Every approval, exemption, requirement, designation, consent, order or other decision made by the Minister or a regulatory authority under the Act must be made in writing and may be subject to conditions. Written decisions, except ones which provide unconditional approval of a request, must state reasons.

Before making a decision, the regulatory authority must give affected persons notice in writing and such a person may require a hearing. Hearings associated with ministerial decisions will be delegated to the Superintendent. Following a hearing, the decision which was originally intended can be confirmed or another decision made in its place. Such hearings are not an appeal but, rather, are part of the regulatory process.

Hearings will be open to the public unless it would be prejudicial. Witnesses may be required to testify under oath and oral evidence may be recorded and transcripts obtained.

Appeals of all administrative decisions of the Superintendent, Council and CUDIC will be to the Commercial Appeals Commission. An appeal will not stay a decision unless the Commission orders the decision to be stayed. Appeals of ministerial decisions may be made under the terms of the Judicial Review Act.

CHAPTER 17

PENALTIES

POLICY

The FIA will have two-tiered offense provisions which set out those specific sections of the Act that a person may be prosecuted for breaching. Relatively low maximum penalties will be set for less serious offenses, but significant maximum penalties will be available for potentially serious offenses.

DISCUSSION

The objective of this policy approach is to strike a balance between effective deterrence and the barrier which may be imposed if penalties for minor violations are too severe. For example, the possibility of significant penalties for minor infractions such as late filing may dissuade qualified individuals from acting as directors and officers of financial institutions. This balance will be accomplished both by the two-tiered offense provision and by not including all sections in the list of those which may give rise to an offense. This does not preclude civil liability or regulatory sanctions but there is no justification for quasi-criminal sanctions to be universally applied.

DETAILED APPROACH

Serious Offenses

The following will be considered serious offenses:

- use of misleading advertising or sales practices, the misuse of the terms "guarantee" and "deposit", failure to make required disclosure to customers;
- operation without proper business authorization;
- failure to seek approval for a significant change in the structure or ownership of a financial institution;
- violation of self-dealing rules by a person who knew or ought reasonably to have known the rules were being violated;
- deliberate breach of investment standards or impairment of capital;

DETAILED APPROACH (Continued)

Serious Offenses (Continued)

- disobedience of an order of the Minister or Superintendent; and,
- deliberate provision of false information to the Minister or the Superintendent or failure to provide the Superintendent or auditor with access to information in accordance with the Act.

Maximum penalties currently under consideration are imprisonment of up to two years or a fine of up to $100,000 for a first offense and imprisonment of up to two years or a fine of up to $200,000 for subsequent offenses.

Other Offenses

Other offenses will also be specifically listed and will include:

- failure to file or provide notification as required;
- violation of referenced provisions of the Company Act;
- failure to account for or maintain statutory trust funds or accounts properly;
- failure to maintain confidentiality of customer information;
- failure to obtain mandatory director training;
- insufficient unaffiliated directors; and,
- other similar offenses.

Maximum penalties currently under consideration for these offenses are, in the case of a corporation, a fine of up to $5,000 and, in the case of an individual, a fine of up to $2,000.

Other Provisions

The limitation period for the commencement of proceedings in court for offenses will be two years from the time the facts first come to the knowledge of the Superintendent or other regulatory authority. This limitation period will also apply to offenses against the Company Act by or related to a financial institution.

DETAILED APPROACH (Continued)

Other Provisions (Continued)

Where a corporation is guilty of an offense, any director, officer, employee or agent of the corporation who knowingly authorized, permitted or acquiesced to the offense will also have committed an offense.

In addition to any penalties imposed on a person convicted of an offense, the court will be empowered to order the person to comply with the Act and/or order the person to pay restitution.